

Audit Committee Chairman's Letter

The members of the Audit Committee are selected by the Chairman of the Board of Governors. During 1998, the Committee, consisting of myself, Governors Ballard and McWherter, met seven times in conjunction with the regularly scheduled monthly Board meetings.

The Audit Committee is responsible, on behalf of the Board of Governors, for reviewing the financial reporting process, ensuring the soundness of the accounting and control practices, and the integrity of the financial statements of the Postal Service. As a part of that responsibility, the Committee also reviews other related issues as appropriate.

The Committee also recommends to the Board of Governors, subject to its approval, the selection of the independent public accounting firm responsible for the external audit work and oversees compliance with the terms of the contract.

During 1998, the Committee recommended and the Board approved changes to the Board's Audit Charter which were necessary to recognize the shift in audit responsibilities from the Inspection Service to the Office of the Inspector General.

The Committee discussed the overall scope of the work and the specific audit plans with the external auditors, Ernst & Young LLP, the Office of the Inspector General and the Postal Inspection Service at the start of the audit process. We also met regularly with management, the Inspector General, the Inspection Service, Ernst & Young, and the General Counsel jointly and, as appropriate, independently to discuss the progress of the audit work. This included an evaluation of the organization's internal controls and the quality of the financial reporting process. This also provided the opportunity for the Committee to assess the coordination of the audit work and ensure the independence and objectivity of the internal and external audit programs.

Accordingly, the Committee recommended and the full Board approved the financial statements for 1998.



Einar V. Dyhrkopp
Chairman, Audit Committee
December 8, 1998

Report of Independent Auditors

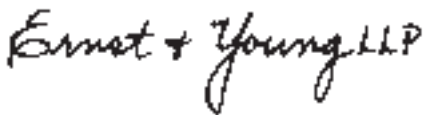
Board of Governors
United States Postal Service

We have audited the accompanying balance sheets of the United States Postal Service as of September 30, 1998 and 1997, and the related statements of operations, changes in net capital deficiency and cash flows for each of the three years in the period ended September 30, 1998. These financial statements are the responsibility of the United States Postal Service's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards and the standards for financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the United States Postal Service at September 30, 1998 and 1997, and the results of its operations and its cash flows for each of the three years in the period ended September 30, 1998, in conformity with generally accepted accounting principles.

In accordance with *Government Auditing Standards*, we have also issued a report dated November 10, 1998, on our consideration of the United States Postal Service's internal control over financial reporting and on tests of its compliance with certain provisions of laws, regulations, contracts, and grants.



Washington, D.C.
November 10, 1998